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# EDITED TRANSCRIPT

VZ - Q1 2020 Verizon Communications Inc. Earnings Call

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## OVERVIEW:

Co. reported 1Q20 consolidated operating revenue of \$31.6b, GAAP EPS of \$1 and adjusted EPS of \$1.26.



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## CORPORATE PARTICIPANTS

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## PRESENTATION

### Operator

Good morning, and welcome to the Verizon First Quarter 2020 Earnings Conference Call. (Operator Instructions) Today's conference is being recorded. (Operator Instructions)

It is now my pleasure to turn the call over to your host, Mr. Brady Connor, Senior Vice President, Investor Relations.

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### Brady Connor - Verizon Communications Inc. - SVP of IR

Thanks, Brad. Good morning, and welcome to our first quarter 2020 earnings conference call. This is Brady Connor, and I'm here with our Chairman and Chief Executive Officer, Hans Vestberg; and Matt Ellis, our Chief Financial Officer.

As a reminder, our earnings release, financial and operating information and the presentation slides are available on our Investor Relations website. A replay and transcript of this call will also be made available on our website.

Before we get started, I'd like to draw your attention to our safe harbor statement on Slide 2. Information in this presentation contains statements about expected future events and financial results that are forward-looking and subject to risks and uncertainties. Discussion of factors that may affect future results is contained in Verizon's filings with the SEC, which are available on our website.

This presentation contains certain non-GAAP financial measures. Reconciliations of these non-GAAP measures to the most directly comparable GAAP measures are included in the financial materials posted on our website. The quarterly growth rates disclosed in our presentation slides and during our formal remarks are on a year-over-year basis, unless otherwise noted as sequential.

Now let's take a look at consolidated earnings for the first quarter. In the first quarter, we reported earnings of \$1 per share on a GAAP basis. Reported first quarter earnings include a pretax loss from special items of approximately \$1.4 billion, including a loss on spectrum licenses related to Auction



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103 of \$1.2 billion and a net charge of \$182 million related to a mark-to-market adjustment for our pension liability. Excluding the effects of these special items, adjusted earnings per share was \$1.26 in the first quarter, up 5% compared to \$1.20 a year ago.

Let's now move to Slide 4 and take a closer look at our first quarter earnings profile. We expect 2020 to be the final year that the adoption of accounting standard ASC 606 for revenue recognition will have a material year-over-year impact on our income statement. As we illustrated in previous quarters, we realized a lesser benefit from the adoption of ASC 606 during the first quarter compared to the prior year, primarily due to the deferral of commission expense. The reduction of the benefit realized creates a year-over-year headwind to both reported and adjusted earnings per share, which will continue throughout 2020. The impact was \$0.03 for the quarter.

For full year 2020, we expect headwinds from the deferral of commission expense to be approximately \$0.09. We estimate there was a negative \$0.04 net impact included in the reported and adjusted EPS from COVID during the quarter. Matt will go through this in more detail later. Adjusted EPS growth of 5% over the prior year, illustrated on the earnings waterfall slide, reflects the strong underlying performance of the business, partially offset by the impacts of the deferral of commission expense.

With that, I'll now turn the call over to Hans to walk you through a recap of the actions we have taken during this unprecedented time.

### **Hans Vestberg** - Verizon Communications Inc. - Chairman & CEO

Thank you, Brady, and most welcome to this earnings call. This is an earnings call that is very different from all previous ones that I have done. I've been in crisis -- in the telecom crisis in 2000, bank crisis in 2008 and '09. This is something totally different. It's a health crisis with a pandemic that impacts each and every one of us wherever you are in this world.

I'm proud of the team of Verizon, how we have been stacking up in this crisis and how we work together. We decided very early on to split our team, in our crisis management team, and the leadership team continue to drive our business forward. In the middle of February, we made that split in order to see that we're actually attending all the things that happening in a company the size of Verizon.

Our COVID-19 response has been based on how we manage our 4 stakeholders. We have taken decisive action, but they're all balanced and thinking about the long-term and positive impact for all our stakeholders. Let me quickly go over what we have done in different areas of stakeholders.

On the employee side, the majority of our all employees are working from home. We moved quickly to a work-from-home environment. Today, we have high productivity in that setup. We have also retrained some 20,000 of our own employees to work with new tasks and work from home. And some additional 1,000 of third parties that is part of our delivery.

But also, we need to acknowledge we have a lot of our employees in frontline, serving customers, keeping up the networks, at the same time as keeping some of our stores open. We have roughly 30% of our stores open, of course, with limited opening times and also only by appointment. But they are playing a vital role to keep up the most important infrastructure in this country right now, besides hospitals and first responders, and I'm happy to report the team is doing a great job.

And talking about our customers, we have been attending all our customers with new demands during this crisis. At the same time, we are also part of the pledge of Keep Americans Connected, which means that we are waiving late fees or overages for small and medium businesses and the residential customers that have been impacted by the coronavirus.

Our network has performed well. I will come back to that a little bit later.

When it comes to our work in the society, helping communities, that's also extremely important right now. Large corporations need to take the responsibility. We have done some of it, like the PayItForward, which is our concert twice, sometimes 3 times a week, which is gathering concerts or celebrities, bringing in people actually adding to and helping small and medium businesses. We call it PayItForward LIVE. But also work with WHO and other organization that needs help and ultimately supporting the most vulnerable in our society.



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Finally, on the education side, that we always have been focused on, we're not only supporting the schools that had already had their support for, but we're also adding together New York Times, offering all the content from New York Times to all the high school students across the country. So we're proud what we're doing in that area.

And finally, on the financials, we have also worked quite a lot with what we're doing in our cost side. We're taking already cost measurements in the first quarter, everything from third-party spending, seeing, of course, that we're traveling less but we're doing this prudently as usual. On top of that, we increased the CapEx guidance in the quarter because we felt that it was a good time for us to continue to see that we have robust networks as we went into a moment in time we don't really know how the network would be used. At the same time, of course, sending a message that we think is a good return on investment on that incremental CapEx. At the same time, I think Matt and his team has done a great job of seeing that our balance sheet is in the best shape, added liquidity in the middle of the quarter through very cost-effective bond costs that we had.

And we are also working with scenario planning. Nobody really knows how this is going to end, but we have several scenarios and actions that we're working with as a leadership team.

Let me talk about the network a little bit, and we have been reporting every week the development of our network since the outbreak of the pandemic. And you are seeing some staggering numbers, like over 200% up on gaming, 10x up on collaboration tools, 40% up on video. 800 million calls a day, which is twice the amount of what we have on Mother's Day, which is the biggest day a year. All that we have been managing very well with the network. We have built a robust network, and we can deliver high quality.

If we then look now week-to-week, you can see on the slide that we have much less of changes. We feel that we have settled in on the type of usage of the network and where it's used. So it's very small variation.

I just want to point out the mobile handoffs, which is basically how our customers are moving between different cells, down 35% since the outbreak of the COVID-19. And in certain places like New York City, it's over 50% reductions on mobile handoff.

So how our network hold up then when it comes to all those changes? This is how we showed during the Investor Day, the -- how our capacity versus the busy hours in the wireless network. As you can see, we continue to keep the same headroom in the network when we come into the COVID-19. And the main reason is that, first of all, we were prepared. We have added capacity. But also the network is using different time frames and with different applications. And this exclude any use of the AWS-3 temporary spectrum that FCC so greatly lent to us in the beginning of this crisis as an insurance if usage would go somewhere we wouldn't know. But however, I can report that our technicians and our operations team has done a fantastic job, and the network is keeping up very well with the changes and the enormous usage of the network.

Let me just finish up before I hand over to Matt and talking about the progress towards our 2020 commitment. They are intact. We work to see that we can both handle this crisis, which is unprecedented, but we also continue to execute on our strategy. When it comes to strengthen our core business and grow our core business, of course, we, right now, have more digital sales than we had before, which is, of course, very encouraging. But we also strengthened our core business by adding a very good and nice piece of millimeter wave spectrum that gives us very good holdings for fortified strategy.

When it comes to leverage our assets, and we're growing in the future, our 5G plans and our fiber plans, the build out of that are on plan. We were also a little bit ahead of plan when we ended the first quarter. And can I report still today, we are on plan with the 5G and fiber. Of course, our challenge is out there when it comes to COVID-19 and so on. But our team are finding new ways and innovative ways to actually do the deployment. There are ways of dealing with approvals from the municipalities set by new ways. And we have great collaborations from many of the municipalities to do it. There might be problems going forward, but I am also confident that my team are very innovative in the field and see that we continue to drive hard on this.

We also added an acquisition just recently, the BlueJeans acquisition, adding to what Matt and I said in the fourth quarter, talking about the investment we want to do in our Verizon Business Group, where we see great opportunity and, of course, then accentuated in this COVID-19 where we now add the BlueJeans capabilities, both to our existing distribution, but also for the future of 5G, where we think there are video capabilities



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that's going to be extremely important. On the financial discipline, we continue to drive that. Matt is leading that work, both preplanning and what we're doing.

And finally, about our purpose-driven company, which is so important this time to see that you have all your employees with you. We are doing a lot of impact in the society. We have virtual volunteering right now, where a lot of our employees can actually contribute to the society in these tough times. And finally, we also actually communicate with our employees basically every day on a live webcast in order to see that everyone knows what we're doing and where we're going in times of uncertainty.

Quickly, on the first quarter. Matt will cover it much better. I'm proud of the team, delivering strong growth in wireless service revenue but also the 5% growth on our adjusted earnings, which includes impact of COVID-19 and then a strong cash flow, up 26% year-over-year. The segments all had their challenges, but also their strength in this quarter. Mainly, the challenges come from COVID-19.

Finally, on the guidance, we decided to continue to do certain guidance, even there are certain unclarity in the market and of the future. We decided that revenue, we will not guide on the revenue because the hardware is so hard to predict at this moment. But we actually are guiding on EPS and continue with all other items as well. And Matt will go through that in detail, but always with the understanding that we don't have all the knowledge what will going to happen. We may need to make assumptions about it.

By that, I hand it over to Matt.

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**Matt Ellis - Verizon Communications Inc. - EVP & CFO**

Thank you, Hans, and good morning, everyone. As Hans discussed, we are in an unprecedented time. As a result of the impact of the COVID-19 crisis and the various measures taken to address the emergency, we experienced starkly different trends during the first 2.5 months of the first quarter than we did during the last few weeks. We understand that most of you are more interested in what we are currently seeing in the business, so I'll go through the quarterly results at a high level and spend more time addressing the most recent trends and how they impact our expectations for the second quarter and the full year.

We will begin with a review of our consolidated operating and financial results. In the first quarter, consolidated operating revenue was \$31.6 billion, down 1.6%. Growth in wireless service revenue in both the Consumer and Business segments was offset by sharp reductions in equipment revenue. Consolidated wireless equipment revenue was down over 16% in the first quarter, driven by the Consumer segment, primarily as a result of the limited in-store customer engagement in March due to COVID. Adjusted EBITDA was \$11.9 billion, down slightly from last year, including the impact from COVID. Low wireless volumes in Consumer Group drove benefits to margins through decreased promotional spend, lower equipment revenue and improved churn. These benefits were more than offset by higher bad debt expense, lower advertising revenues from Verizon Media Group in March and customer actions that resulted in a decrease in wireless fees and nonrecurring usage charges. Our incremental bad debt reserve of \$228 million was the largest component of these items.

The headwinds from the deferral of commission expense, that Brady highlighted earlier, reduced EBITDA by \$172 million, which is an impact of approximately 55 basis points to EBITDA margin in the quarter. We have continued to focus on our Business Excellence program, with the goal to realize \$10 billion of cumulative cash savings by the end of 2021 and have saved \$6.3 billion through the end of the first quarter. The activities of this program over the past 2 years have put us in a position to be more agile and adaptive in uncertain times like these.

Adjusted EPS for the first quarter was \$1.26, up 5.0% from \$1.20 a year ago. This included an estimated net impact from COVID of approximately \$0.04, primarily driven by an increase of our bad debt reserve.

Let's now turn to our segment results, starting with Consumer Group on Slide 10. Our Consumer team continues to deliver best-in-class services to our customers while keeping them connected in their personal and work communities. We are extremely proud of the team's performance, particularly our frontline workers' efforts to meet our customers' needs during this very difficult period. Our Consumer segment started the year with typical low seasonal volumes during the first quarter. In March, customer transaction activity slowed significantly due to shelter-in-place



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policies, travel restrictions and other measures taken to promote social distancing. Later in the call, I will go into a deeper discussion on the exit rate trends as we serve our customers in this new environment.

First quarter phone gross adds were down nearly 13% year-over-year, and postpaid phone net losses were just over 300,000 for the quarter. Phone churn performance was solid throughout the quarter at 0.77%, which was down 4 basis points from a year ago. Consistent with first quarter seasonal volume activity and the impact of COVID, our retail postpaid upgrade rate remained low during the quarter and is one of the key contributing factors to the decline in wireless equipment revenue. We expect this trend to continue for as long as social distancing policies and other safety measures to protect our employees and customers continue to limit store traffic.

Fios Internet net additions of 59,000 were up sequentially and year-over-year as work from home, in-home schooling and other related measures increased the utility and demand for our high-quality broadband offerings. Fios video net losses accelerated for the quarter, and we expect cord cutting trends to continue. In order to ensure the safety of our customers and employees, while providing critical network services, we have modified our approach over the past few weeks and are not currently entering customer locations, except for critical functions.

Now let's move to Slide 11 to discuss the Consumer financial performance. Our Consumer segment entered 2020 with strong momentum as we added a significant number of wireless connections towards the end of 2019, which favorably impacted the first quarter. For our Fios consumer products, we launched new Mix & Match pricing early in the quarter, providing price transparency and choice in our broadband and video offerings. We also introduced Yahoo Mobile to expand our wireless offerings across our digital media customer base. We continue to generate strong service revenue and other revenue growth. But this was more than offset by a significant decrease in wireless equipment revenue due to low volume activity.

Consumer segment total revenue was down 1.7% year-over-year. The growth in unlimited plans, increase in connections per account and high demand for our broadband services in the quarter drove strong profitability for the segment, offset by an increase in bad debt expense as a result of COVID impacts. Consumer EBITDA margin of 46.4% was up 60 basis points over the prior year and included approximately 80 basis points of headwind from the deferral of commission expense. Lower equipment revenue had a limited impact on our overall EBITDA performance.

Now let's move to Slide 12 to review the Business Group results. During a time when connectivity is providing critical support to those impacted by this crisis, our Business team is at the forefront to serve our enterprise, small and medium business, public sector and wholesale customers. We remain an outstanding partner for first responders, health care providers and other frontline workers. And as Hans mentioned, we are extremely proud of our team's work to deliver essential services to our customers so they can serve others. Business trends were strong throughout the quarter, and we saw heightened demand for our products and services in March. Businesses need our services now more than ever, as we saw strong demand for mobility, Jetpacks, VPN services and high-speed circuit capacity in the first quarter.

As you look at the detail on the slide for wireless products, you can see phone gross adds were up 25% from the prior year, driven by strength in global enterprise and public sector, with offsetting pressure in small and medium business. This contributed to postpaid phone net adds of 239,000 and total postpaid net adds of 475,000. Business segment phone churn of 1.02% in the quarter was flat year-over-year, driven by strength in public sector, with offsetting pressure in small and medium business.

Let's now move to Slide 13 to review the business financial performance. Operating revenues for the Business segment in the first quarter were down approximately 0.5% from the prior year. Wireless revenues within enterprise, SMB and public sector were up year-over-year, driven by strong wireless service revenue growth of 6.9%. This was offset by legacy wireline and wholesale revenue declines. We are encouraged by the business EBITDA performance in the first quarter, which was driven by tight controls around spending and strong wireless performance as we generated solid profitability, even with higher-than-usual volumes and the ongoing transformation investments in the segment for future growth.

Now let's move on to Slide 14 to discuss Verizon Media Group. During the first quarter, Verizon Media Group's performance was impacted by COVID, similar to others in the digital advertising and search business. Total revenue is \$1.7 billion, down 4% compared to last year, driven almost entirely by COVID impacts. Prior to COVID, our year-over-year revenue trends were continuing the steady improvement seen in 2019. We are seeing increased levels of customer engagement across our platforms. But advertising rates and search revenue have declined in the current environment.



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Verizon Media launched a coronavirus hub on Yahoo! News and Yahoo! Finance and COVID-19's newsletter through Yahoo Mail, both of which are driving significant customer engagement as we aim to keep users informed on what is happening in their area and around the globe with trusted content.

Let's now move to Slide 15 for a quick look at the overall wireless performance. Slide 15 shows the key metrics and financial data of the combined wireless products and services from the Consumer and Business segment for the first quarter. Total wireless service revenue grew 1.9% over the prior year. Additional details are provided in the financial and operating information and our supplemental earnings release's schedules on our website.

Now let's review our cash flow and balance sheet for the quarter on Slide 16. Cash flow from operating activities was \$8.8 billion, an increase of \$1.7 billion from the prior year. This year-over-year growth was partially driven by Voluntary Separation Program payments and the voluntary pension contributions in the first quarter of 2019 that did not repeat this year as well as working capital improvements from our operations this quarter. Capital spending for the first quarter totaled \$5.3 billion, which is up approximately \$1 billion year-over-year. We expect the timing of capital spending to be more front-end loaded than it was last year. Our capital expenditures continue to support capacity for unprecedented traffic growth across our networks while we continue to deploy more fiber and add additional cell sites to support our 5G rollout.

As we mentioned earlier in March, we increased our full year 2020 CapEx guidance to \$17.5 billion to \$18.5 billion in order to facilitate Verizon's network activity and help support the economy during this period of disruption. Free cash flow for the quarter was \$3.6 billion, which was up 26.2% year-over-year and continues to fund our dividend. Our balance sheet continues to be strong, with very low unsecured bond maturities through the end of 2021. Our net unsecured debt-to-adjusted EBITDA ratio was 2.1x, up slightly from year-end.

Let's move on to Slide 17 to take a deeper look at the trends we have seen in the last half of March and into early April. During the month of March, as COVID safety measures were implemented with new federal and state recommendations for social distancing, our retail consumer and small business activity diminished significantly. By the middle of March, we saw a dramatic shift in customer behavior as stores closed and other business activity halted across the country. At the same time, we experienced increased demand from our public sector and some large enterprise customers to support frontline crisis responders, new work from home and home schooling arrangements and other demands for critical connectivity services.

This slide provides selected metrics from March 15 through April 15 and offers a more in-depth view of the early impacts of the current COVID environment. At this point, it is unclear how long these trends will continue.

In our Consumer Group, we closed nearly 70% of our company-operated retail stores and reduced in-store services throughout the day for social distancing safety measures. As you can see on this slide, we experienced a significant drop in customer activity and device volumes during this period. Consumer wireless gross adds declined nearly 50% from the same period in the prior year, and upgrades declined over 40%. As expected, lower customer switching across the entire industry has led to a significant improvement in phone churn.

As part of the industry's effort to help customers, we signed the FCC's Keep Americans Connected Pledge in March and will waive any late fees and keep customers connected in the event of nonpayment due to the pandemic for the period of the pledge. We have added 15 gigabits of data to metered consumers and small business plans and also to hotspot usage for unlimited plans. This additional data, along with increased in-home WiFi usage, has resulted in lower data overage revenue in the quarter. In addition to these customer-focused actions and impacts, consumer behavior has changed dramatically over this short time period, such as reduced international roaming revenue.

In order to keep our employees and customers safe through social distancing, we are generally not performing installations for consumer Fios when work inside the home would be required. Gross adds are currently limited to those that can be performed directly by the customer or with the technician working outside the home.

In our Business group, we have broken out the trends for our small and medium business customer group, showing the drop-off that we have seen in gross adds and upgrades as a major portion of small businesses have seen a steep reduction in activities and, in many cases, a full shutdown. In contrast to Consumer, we are not seeing the same improvement in churn at this time.





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For public sector and some global enterprise customers, we have seen an increased demand for remote connectivity solutions as a greater number of people are working and schooling from home. Wireless gross adds for these customers were up 163% over the similar period in the prior year, mostly driven by demand for phones, Jetpacks and other connected devices. Our network superiority and long-standing relationship with enterprises, first responders and other workers in the front lines has given us the ability to support their connectivity needs across the country when they need Verizon most. In addition to the increase in gross adds activity, we have seen an improvement in retention for our enterprise and public sector customers with phone churn improving by 35 basis points during this period.

We are working with all of our customers during this time to ensure they stay connected, even if they're experiencing financial hardship as a result of COVID. We believe that our enterprise, public sector and wholesale customers will be relatively less impacted than our SMB customers initially, but we may see increased long-term risk from the crisis. Wireless service revenues in our Business Group are being impacted by reductions in overage fees, a reduction in international roaming and an increase in suspension of lines. Across Consumer and Business, we believe total wireless service revenue growth could be 3 to 5 percentage points lower than originally expected in the second quarter as a result of the reduction in fees and usage-based revenues. Additionally, bad debt expense increased as a result of our changing expectations around customer payments during this time. In the first quarter, we increased our bad debt reserve by \$228 million based on the expected number of customers who will avail themselves of payment relief under the Keep Americans Connected Pledge. We will continue to monitor Consumer and Business payment behavior, and we'll work with our customers to help them stay connected despite difficult circumstances. As a result, it is possible that additional bad debt reserves may be required in the second quarter.

In Verizon Media, we are experiencing a decline in advertising and search revenue as advertisers pause, hold back or cancel campaigns during this time and users are searching for fewer commercial terms, providing us with less opportunity for monetization. As a result, advertising revenues declined by nearly 10% in the month of March, with COVID mostly impact in the second half of the month, and that rate of decline has increased in April. A number of industry forecasts expect a 20% to 30% decline in digital media revenues in 2Q, and Verizon Media's results are likely to be similar to those experienced in the broader industry.

Now let's go to Slide 18 to discuss our guidance and outlook for 2020. Obviously, the environment we find ourselves in today is vastly different than when we originally gave guidance just a few months ago. Given the unprecedented magnitude of the conditions we have all experienced, we are updating our financial guidance for the full year. We remain confident in our strategy, our business model and our ability to generate sustainable long-term earnings growth. Our consolidated revenue guidance of low to mid-single-digit percent growth that we announced in January included the expectation that 2020 equipment revenues would not create similar year-over-year headwinds as it has in the past few years. However, device activations have been low since mid-March, and we expect that to continue throughout the second quarter, with uncertainty around customer behavior for the remainder of the year. The wide range of potential outcomes around equipment revenue led us to determine that it is prudent to withdraw our consolidated revenue guidance at this time. For adjusted EPS, we are revising our original guidance of 2% to 4% growth and are now guiding to a range of negative 2% to positive 2% change from the prior year. Our new estimated range is based on a scenario that assumes significant headwinds prevail throughout the second quarter. We have limited visibility into the second half of the year, which will depend on various potential operating environments. We will continue to assess the impact of COVID on our business, including our bad debt reserve, and expect to provide an update on our next earnings call based on how things develop between now and then.

Other income statement items for which we provided guidance, including depreciation and amortization, interest expense and the adjusted effective tax rate, remain intact as originally guided. As we mentioned earlier, we have maintained our CapEx guidance for the full year that we announced in March. Our supply chain remains strong, and we have not seen a material slowdown in the sourcing of necessary equipment from our network and device partners.

We are optimistic that the measures government agencies have taken will provide support to citizens, businesses and the frontline responders that have been impacted by this crisis. We remain keenly focused on doing our part to provide best-in-class network performance and customer experience to all of our customers, which will continue to drive long-term operational and financial success, while weathering short term disruptions. Despite the extreme nature of what the world is experiencing, we believe that Verizon is well suited to remain resilient through this situation.

Let's take a look at Slide 19 to discuss our strong balance sheet and liquidity position. Over the past few years, we have strengthened our balance sheet, and the results of those actions have put us in a good position to manage through the impacts of the COVID pandemic. We ended the first





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quarter with \$7 billion of cash on hand. Carrying a higher cash balance during a market crisis is part of our liquidity planning strategy, and we executed on that strategy with a \$3.5 billion bond offering completed in March. In addition, we started and ended the first quarter with no commercial paper outstanding but have accessed this market in the second quarter to further enhance our liquidity. During the first quarter and before the market disruption, we also completed one of our largest device payment securitizations of \$1.6 billion.

Having a cash cushion is prudent right now for many reasons, including our expectation that certain customers may have difficulty making timely payments as a result of the crisis. We are closely monitoring these trends with regard to their impact on our ABS programs.

In the second quarter, we had some nonrecurring cash outflows including \$2.7 billion of maturities and \$1.3 billion of spectrum licenses from Auction 103. Scheduled unsecured bond maturities for the rest of 2020 are 0 as a result of our continued liability management strategy that keep near-term maturities low. Additionally, at the end of 2019, given our funded status and prior discretionary contributions, we expect no mandatory contributions to our pension plan until 2026, subject to market conditions. Our pension funded status has been further protected in recent years as we have increased the hedge ratio of our liability to about 50%. This resulted in the funded status of our pension plans only declining from 92% at year-end to 87% at the end of first quarter. Our standby credit facility with our bank group of \$9.5 billion provides further assurance of our liquidity.

Our balance sheet is strong, and our liquidity position has been further strengthened as we navigate this difficult period for our customers and the markets. We have demonstrated the ability to access the bond and commercial paper markets in recent weeks. Our strong financial position gives us confidence to continue to invest, while also supporting all of our stakeholders.

I'll turn it back over to Hans to provide a look at our 2020 priorities, and then we'll get to your questions.

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### **Hans Vestberg** - Verizon Communications Inc. - Chairman & CEO

Thank you, Matt. Let me just round this off with our priorities going into this year and in the future.

First of all, I feel that we're very well positioned to execute both in the near term and the long term to create more value for all our stakeholders. We have the Verizon 2.0 transformation, which is a new leadership, a new network technology, a new go-to-market, and we are delivering on that. And I feel that we have good results already right now, but more to come. I think we also have a very good strategy around the COVID-19 response that is covering all our stakeholders in a balanced way in order to create long-term value for all of them.

The 5G is still very much in the middle, the center of our strategy. And as you heard me saying before, we're in the middle of the execution, and we're not halting that. We're keeping it up all the time, and the team is doing great work there. And we see opportunity with 5G going forward, both with building all the cities, the 5G mobile edge compute as well as making this nationwide 5G still this year.

Matt talked about our discipline and the financials and our capital position and our capital allocation, I feel good about that. We have done tremendous, not in the last 12 months, but also the last 3 months, in order to put us in a good situation to continue to meet all the demands in our capital allocation, all the way from our business, to our shareholders, to our debt holders.

And ultimately, I think the strong brand that we have has been reinforced in times like that, both by the talent we have, but also by the response to our business practices and the way we're dealing with our society.

So all in all, I feel good about our strategy. I think that we are in the middle of execution of it. We need to have a multipronged strategy where we're managing the crisis at the same time, but that doesn't mean we should not execute on our strategy.

So by that, I hand it back to you, Brady.



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**Brady Connor** - *Verizon Communications Inc. - SVP of IR*

Thanks, Hans. Brad, we're ready to take questions.

## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Our first question comes from Brett Feldman of Goldman Sachs.

**Brett Feldman** - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

A question about your updated EPS guidance. As you noted during your presentation, certain activity in the business has declined significantly. I would assume that there's a degree of cost savings associated with that. You also highlighted some areas where you're seeing some pressures. You highlighted roaming revenues as an example. So I was hoping you can maybe just give us a little more insight into the puts and takes that caused you to see a slightly lower outlook for earnings over the course of the year.

And then just point of clarification, you said that this revised outlook reflects headwinds you expect to see in the second quarter. I'm curious whether you're saying that the variance in earnings that you expect to report this year will primarily be contained to the second quarter. Or if you're saying that those headwinds for the remainder of the year collectively result in a change?

**Matt Ellis** - *Verizon Communications Inc. - EVP & CFO*

Brett, thanks for the question, and good morning, everyone. So as you look at the guidance, and we went through some of it in the prepared remarks. But as you look at the items that are in there, when I think about the revenue side for the second quarter, really break it up into 2 major buckets. You think about the actions that we've taken and the actions -- or the impacts of changes in customer behavior.

So as I start to off and think about the actions we've taken, it starts with, obviously, the Keep Americans Connected Pledge for that 60-day period. The vast majority of that is in the second quarter, and so we'll see more impact in Q2 than we saw in Q1. Additionally, as we mentioned, we've given customers an extra 15 gigabits of data. And whether that be on metered plans or on hotspots for those customers who are on unlimited plans. So that's going to have a significant impact on the overage fees that we would normally collect. Earlier this week, we announced that we would be extending that 15 gigabit from the end of April through the end of May.

On the customer behavior side, one of the obvious ones is obviously international roaming. I think it's fair to say you can put a pretty low number in your model for international roaming revenue for the second quarter. But also, in there, as we think around especially in the SMB side of the business, we would expect to see those customers suspending some of the lines on their accounts over this time period, and that will have an impact on revenue, too.

So when we add all those things up, we see that those should impact the year-over-year service revenue growth in kind of the 3% to 5% range in Q2. Some of those things will obviously extend beyond Q2. Some of the things may not extend beyond Q2. Obviously, we control how much we extend the actions. The customer behavior will obviously be impacted by more of the macro environment, so we'll see how that plays out into the second half of the year.

So you have that there on the service revenue side. As you think about other parts of revenue, obviously, equipment revenue will be down. But also within media, as I mentioned, we're seeing a significant reduction. We were down 4% for the first quarter, but 10% in March. So basically, all of the year-over-year decline in the first quarter was contained in the COVID period. And then as we've gone into the sharp-turned second quarter here, we're seeing those reductions increase. So a lot of the industry forecast is 20% to 30% reduction on \$1.7 billion of quarterly revenue. That's obviously a material number, too.



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So we have some benefits come through on the expense side, but obviously, those revenue impacts are going to impact the overall profitability in the quarter. And you see that reflected in our guide.

In terms of the back half of the year, really too soon to tell. I mean there's a lot of things that play out here over the course of the next 90 days. We'll have a much better sense of what the back half of the year looks like. And then obviously, we'll update our view on that when we get to the next call. But we're optimistic.

What we -- that's what we don't know. What we do know is we come into this situation in a position of strength. We've had good performance in the business over a number of quarters now. We come in with products and services that are obviously very important to customers. And we come in with a balance sheet that we've worked on significantly over the past few years. It gives us a little bit of a shock absorber, if you will, so that we can keep operating our business and position ourselves to come out on the other end of this situation for a position of strength. So that's how we're kind of seeing the second quarter and as we look forward to the rest of the year ago here, Brett.

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### Operator

The next question comes from John Hodulik of UBS.

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**John Hodulik** - *UBS Investment Bank, Research Division - MD, Sector Head of the United States Communications Group and Telco & Pay TV Analyst*

Great. Maybe just as a follow-up to Brett's question on that 300 to 500 basis points. Matt, can you give us any more color in terms of maybe the sub-impact and the ARPU impact that you expect to see from all these different pieces? I mean you gave some great detail on what's going on in April here. Maybe just a little bit sort of a total gross add impact that you expect to see? And then maybe on the ARPU side, how big these components are that are being affected? And how that could potentially play out in that sort of 1% to 3% service revenue decline you're expecting?

And then maybe a new topic on the Fios side. When did you guys start the new policy of not entering consumers' homes? And I saw -- I think you -- it shows here that Internet net adds are definitely slowing, but do you expect that to go negative? And then what do you see for video trends as we look out into the second quarter?

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**Matt Ellis** - *Verizon Communications Inc. - EVP & CFO*

Yes. Thanks, John. So following up on the service revenue. When you think about the ARPU, you've got the base billing, and then you've got the additional things that go in there, whether that be international roaming, whether it be overages, whether it be late fees or whatnot. So we feel really good about the core billings within the business. We're seeing customers use our products and services, obviously, on a -- in a very strong fashion and I should expect to see that continue. But where we will see some pressure is around the edges with those other parts of what we bill, whether as I say, it be roaming, overages or whatnot. So the vast majority of that 3% to 5% comes from those items that we bill that are in the service revenue line. And then on top of that, you'll have the impact of suspends on the SMB side. We'll see how much that plays in.

So overall, most of the -- we will see an impact in ARPU there as we go through the quarter. But subs are looking in a great position, as we mentioned, the churn is at a low level. You're looking at about a 0.5 type of range right now in Consumer. Obviously, that's very low compared to where it has been. And I think it reflects the fact as you go into a time like this, consumers obviously value the quality of their network connection with all the increased activity we've seen across it. So all in all, that's where you'll see the majority of the impacts in service revenue as we go into the second quarter here.

And I'll turn it over to Hans and provide some comments around what we're doing with Fios and the engineers going into consumers' homes and whatnot.

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**Hans Vestberg** - Verizon Communications Inc. - Chairman & CEO

Thank you, Matt. And John, let me say one thing that we have been balancing all the time is, of course, safe and -- safety and health for our employees. And that's why we were very early on to actually close down almost 70% of our stores and go to new sort of visiting hours and all of that.

The same we have done with our engineers in the field, very important for us to see that they are safe and healthy. And in the beginning here, we were very restricted on visited on homes. But we've also seen a lot of innovation. And the last couple of weeks here, we have actually innovated, so we can start installing Fios without going into the homes with both what we call the Fios in the box, which is where the consumer or the customer is installing themselves; as well as we also have a virtual agent right now where the customer can be guided how to do the installation. That innovation, we have been able to do in 2, 3 weeks, and now we start ramping that up. And I'm confident that over time, we almost can be back on a normal levels of installation, but with the safe and healthy of our employees and as well for our customers.

And I think that, again, just coming back to the importance on balancing, in a crisis like this, you need to balance all the different stakeholders and see that you really have the priorities right. And our priority has been from the beginning, the safety and health for our employees. That's very important.

Second is, of course, to see that our networks are staying up because of the importance of our infrastructure in these times. Because we know that the country is needing our network and our technology staying up and having the highest quality as Verizon always has. So we are managing that every day here, and I think we're managing it very well. And as said, the innovation is now telling us and we can go back to something that is normal, but in a totally new way of doing it. So I'm grateful for my team.

**Operator**

The next question comes from Phil Cusick of JPMorgan.

**Philip Cusick** - JP Morgan Chase & Co, Research Division - MD and Senior Analyst

To clarify one more time on this 3% to 5% in 2Q. Can you please confirm that is versus your prior expectation for year-over-year growth rather than just year-over-year? And also, can you quantify what the service revenue headwind was in the first quarter versus the regular business growth rate?

And then second, Verizon Media revenue sounds like down 20% to 30% in the second quarter. What do the margins look like in this business? We don't really know much about what the sort of cost flexibility is there and whether margins can stay positive or flip to negative when revenue comes down quickly.

**Matt Ellis** - Verizon Communications Inc. - EVP & CFO

Yes. Thanks, Phil. So as you look at the service revenue, and you think about the impacts in there, the 3% to 5% is really is going to be 3% to 5% lower than they otherwise would have been. A reduction in the growth rates on a year-over-year basis is what you'll see there.

There was a small impact on service revenue in the first quarter. If you think across both Consumer in the 30 to 40 basis points of service revenue growth so the 1.9% would have had some upside without the impact that we saw at the back end of March. But we're in -- we like where the position of the service revenue trajectory is. As you come into the quarter, as you go into 2Q here, the core underlying performance of the wireless business in both consumer and business is very strong. And we expect to see that show up in our service revenues throughout the rest of the year.

**Hans Vestberg** - Verizon Communications Inc. - Chairman & CEO

Something about the Verizon Media Group. As Matt reported, of course, that we have seen an impact lately on our advertising. We're, of course, encouraged about the increased activity and the growth of engagement because that's ultimately going to pay off later on. And I think that, first



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of all, our Verizon Media team has been extremely innovative with new products and new ways of delivering services the last couple of weeks here in a time of this pandemic.

I have to say that I have a lot of confidence in my Verizon Media Group to work with different scenarios, given how this pandemic will develop and how it will hit Verizon Media Group. We have seen the last 18 months or, I don't know, 6 quarters that our Verizon Media Group has found ways to both reduce direct cost and find new ways to innovate. But all in all, we need to understand that, of course, advertising these days, you are restrictive, you're cautious given the pandemic.

But again, I think that, as I said in the beginning, we are working with different scenarios that can happen, and we have different levers and activities that we can do given where this is going. That goes for all our different businesses, which, of course, they are in different form and shape at the moment, but it also goes for the whole corporation.

And then just adding on what Matt said about our wireless business. I think that one thing that worked in the brand, since we embarked on the unlimited some 2 years ago, we have constantly built a model which can actually meet all the different scenarios, all the way from our Mix & Match, our -- in Visible, Yahoo Mobile, the work we're doing with track phone, the network as a service. I think that regardless where it will go, we will have opportunities to actually serve our customers with the plans that they need. And I think that few others can do that in this market as well as we have the best network. So I think we're well positioned in the world that might be uncertain, but we have all those different type of opportunities to serve our customers.

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### **Matt Ellis** - Verizon Communications Inc. - EVP & CFO

And just real quick on the cost side there that comes, obviously, the service revenue impact and the media revenue impact. But obviously, we're doing things to manage the cost side of the business as we go through this period. And it's really building on the work we've been doing for the last few years now, and it's put us in a position where we can take the actions that we need to in this time. We'll see some cost benefits as we go through this. But it also allows us to do the things to support our employees and customers and to keep investing in the business for the long haul even as we're in this unusual time period. So cost controls are very much on our mindset as we go through this time period as well.

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### **Philip Cusick** - JP Morgan Chase & Co, Research Division - MD and Senior Analyst

If I can just clarify as well on Brett's question. You said that a lot of the impact, I think, for the EPS cuts is in the second quarter. But I think it would make sense that you're guiding for probably weaker earnings through the year. Is that fair?

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### **Matt Ellis** - Verizon Communications Inc. - EVP & CFO

Most of the impact in the guide is the impact that we discussed in the second quarter. As we look to the second half of the year, obviously, there's a very wide range of potential outcomes there. So we'll see how that plays out. And obviously, when we're on this -- the next earning call, 90 days from now, we'll have a lot more to say about the second half of the year. But a lot of the commentary we had and a lot of the updates in the guide relates to what we'll see in 2Q. But we will see some of those revenue impacts, you think about international roaming, for example, will stay with us for a longer time period. But we'll wait and talk more about the second half of the year when we have better visibility into it.

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### **Operator**

The next question is from David Barden of Bank of America.



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**David Barden** - *BofA Merrill Lynch, Research Division - MD*

I guess, 2, if I could, first, just kind of looking at the Slide 17, where you give us kind of the COVID environment effect on the mobile business. Could you give us some of that similar color, Consumer, SMB and enterprise on the wireline side?

And then second, obviously, last quarter, there was a big investment in the business services group in terms of trying to modernize the tech and the go-to-market capabilities. Could you kind of elaborate a little bit on what's been accomplished thus far in that exercise? And kind of what, in the current environment, your expectations might be for the return on that investment at this stage?

**Matt Ellis** - *Verizon Communications Inc. - EVP & CFO*

Yes. Thanks, Dave. That's -- let's unpack those. Starting off with the wireline impact on the current environment. In Fios, we talked a little bit about that. We saw good volumes in Internet in the first quarter, but that was largely a reflection of low churn as we came into this. And obviously, a lot of appreciation from our customer base on the quality of the Fios Internet product.

As you go into the second quarter, you're going to continue to see the benefit on the churn side, but obviously we'll have some impact on the gross adds side from the employee actions that Hans mentioned, where we're not allowing employees to really enter customers' homes.

What's really good -- what you see from us is, say, okay, how do we react to this? So Hans talked about the Fios in a box, right. Let's not let this environment completely stop what we're doing. How do we -- yes, there's an obstacle in our way. Let's find a way around it. This team is phenomenal on doing that. So we will have some gross adds here in the quarter that we might not have expected when we first stopped going into customers' homes.

As you look across the other parts of wireline, as you get into SMB and the larger businesses, obviously, as we've seen an uptick in usage across the core networks and we've been doing a number of things to help, especially our larger enterprise customers adapt very quickly to having their -- a large number of their employees work from home and having to update their systems to be able to handle that change in network traffic and where the work is performed. So I would expect to see a continuation of that. But it won't massively change the ongoing wireline trends -- revenue trends that we've seen across the business as we think about second quarter here.

In terms of the investment in VBG and what you see in the margins in the first quarter there, I think we came in with a decent margin for that group. But as I shared on the call back in January, this isn't a one quarter investment in the business. There's a number of things that we need to do to upgrade the capabilities of our Business group so that we can be that partner of choice for businesses as we enter the fourth industrial revolution. And so there's a lot of good activity going on there. And I'll stick with what I said on the last call that we'll be investing in that for quite a while here. We should start to see the impact -- the benefits on the cost side towards the end of this year. And then the impacts on the revenue side in '21 and really getting full steam in '22, so a lot to come there.

And Hans, I'll let you follow-up on that.

**Hans Vestberg** - *Verizon Communications Inc. - Chairman & CEO*

Yes, you're absolutely right, Matt. This is -- we are clear on the strategy of the Verizon Business Group. I just want to remind all of you, we brought together several different groups on wireline and wireless and this go-to-markets. Tami and the team has very clear strategy of doing the transformation. That has not slowed down. We continue with that because when coming into this COVID-19, we see even a more importance of Verizon Business Group than really Matt talked about. This is one of the areas we see that we have a great opportunity going forward as we build a Verizon Intelligent Edge Network, as we come with 5G and the trends in the industry. I mean, digitalization, all of that, which, of course, has been accentuated in this COVID-19.

So I feel good about what we're doing here. The team is running as fast as they can with this transformation. But as Matt said, this is not the 1 quarter thing, but we're not holding back on the transformation. And in that transformation, we said we will invest, and one investment was, of



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course, the BlueJeans, which we have had in our portfolio for a couple of quarters as a distributor. But as this turned out, we felt that it was a good opportunity to actually make the acquisition, and we have been testing them. It's a great product. And we stitch that into our go-to-market in the Verizon Business Group. But I also see it as a great opportunity for the 5G. Because ultimately, 5G at the edge, we will have a lot of low latency, enormous throughput where video and transcoding will be important. So adding that asset is also important for the future.

So once again, we feel good about our strategy in Verizon Business Group and how they have performed. And we have some more work to be done, and we're not holding back on that transformation as that will put us in even stronger position when they're done.

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**Operator**

The next question comes from Simon Flannery of Morgan Stanley.

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**Simon Flannery** - *Morgan Stanley, Research Division - MD*

Thanks for all the color on the COVID-19. Very helpful. I wonder, Matt, if you could get into a little more on the bad debt, help us understand where that is across the Consumer versus Business. I'm guessing a lot of it's in SMB. How does that break wireless, wireline?

And then, Hans, could you talk a little bit about the digital channels. You talked a lot about Fios in a box. How are you thinking about maybe pushing more of the phone sales and wireless sales through the online channel? Where are you today? And what can you do to increase that percentage?

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**Matt Ellis** - *Verizon Communications Inc. - EVP & CFO*

Thanks, Simon. So on the bad debt, as we look at that, the vast majority of it is sitting in the Consumer side just because of the relative difference in the size of the businesses between Consumer and SMB. As we did the bad debt reserve this year, we're now operating under the new CECL accounting standards. It requires us to take a more forward look at expected losses.

And so really, what we did, we took -- we looked at how many customers have availed themselves of the pledge. We used that as a starting point for the reserve. I can tell you as of around mid-April, we have around 800,000 customers who have signed up for the pledge and some of the various other stakeholders. The vast majority of those are in mobile, and that provided some of the bases. But it's too early to know exactly how the bad debt requirements will play out. We'll monitor that closely here as we go forward.

But certainly, we're seeing different payment patterns across different parts of our customer base. Actually encouraged by what we're seeing on the Consumer side here over the last couple of weeks. And another proof point that as we've talked about in the past, as we saw in the financial crisis, that consumers continue to put their phone bill high up their list of priorities for payments.

And certainly, we're monitoring closely on the Business side, especially within SMB, how that's going to play out. Nothing in the payment patterns at this point is overly pessimistic, but we're obviously going to stay very close to that and work to keep our relationship with our customers wherever possible. So that hopefully gives you a little background on how we look at the bad debt. And I'll let Hans answer the question on how we see digital channels going forward.

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**Hans Vestberg** - *Verizon Communications Inc. - Chairman & CEO*

So let me just lay out how we're running the company right now. We're basically running the company in a 3-pronged strategy. The first prong is, of course, the crisis management, where we have a team that is dealing with all the challenges with pandemic for our employees, for our customers and for the society at large.



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Secondly, I have the majority of my leadership team running business as usual. We have our 5G governance early this week, where we went through all the deployment, all the 5G mobile edge compute, all the new business cases, just running as normal.

And then we have a team, which also think about the new normal. What will be the new normal when we come out from this pandemic? And one of the question, which is, I think, I believe is going to happen, we're going to see much more digital sort of omnichannel from our customers, and we are ready for it. We have already pivot to it. We're probably going to see another environment -- work environment that we need to think about. We're probably going to also see a different type of product that we need to put forward.

So I try to see that we have all these 3 prongs working at the same time in order for us to come up even stronger from this crisis as well as managing the today and not missing our target put up as well as managing the crisis at the same time. So I can only confirm, I have the same feelings as you have. We're going to see much more of digital usage of ordering. But we're also going to see things that we never thought were possible. I mean telehealth will increase over time. People are now and still, they don't need to go to hospital. We're going to see education -- remote education growing because people see that it's actually working. All that's going to be new normal where we -- our assets are extremely important in that delivery to all our customer groups. So you need to work on all 3 of them, and we are working all 3 of them to come even stronger out on this crisis.

### Operator

The next question comes from Craig Moffett of Moffett Nathanson.

### Craig Moffett - *MoffettNathanson LLC - Founding Partner*

I wonder if I could just ask a slightly longer-term question in the context of the COVID crisis. Your investments in wireless, which have largely been -- in 5G, I mean, which have largely been on the back of millimeter wave spectrum, have almost necessarily been in dense, urban gathering places, like stadiums and arenas and airports and what have you, which is obviously where people aren't today. Do you stop and say there may be a real change in social patterns that suggest a different set of investment priorities that are more along the lines of coverage and less around dense urban usage? Or is that likely to be sort of a short-term blip just given how long the planning windows are for network densification? I ask this in the context of a spectrum strategy where it could well be that mid-band spectrum becomes even more important now, given a potential pivot away from those very dense, urban gathering places.

### Hans Vestberg - *Verizon Communications Inc. - Chairman & CEO*

Thank you, Craig. It's still to be seen, first of all, of what will be the social patterns for the time. I feel pretty confident that dense, urban areas will continue to be dense, urban areas. And to be honest, we still see a lot of usage in dense, urban areas. It's just that we see less movement of people because they are staying home. So people live where they live today. So we are not changing the strategy, how we execute, both on the broader nationwide as well on our city deployment. And ultimately, we see that as being a very compelling offering going in the future.

On the mid-band, as I said before, especially on the C-band, we think that is an attractive spectrum because, first of all, as you said, it is a good coverage. But also, it's a global roaming standard for 5G. And of course, we want to be part of that. And we are encouraged by FCC's plan to conduct a C-band auction in December. And we will always do our normal return on investment between the different densifications, buying spectrum, putting more software and keeping in mind that we want to continue to have the same headrooms in the network as we always have in order to have the best network.

So yes, it plays in. It's a little bit too early to say that we're going to have a changed total social pattern in the United States. Initially, I don't think so. People live where they live, and that's going to continue to be the same.



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**Craig Moffett** - *MoffettNathanson LLC - Founding Partner*

And can you comment specifically about the L-band uplink concept and the availability now of Ligado spectrum?

**Hans Vestberg** - *Verizon Communications Inc. - Chairman & CEO*

Yes, I can, or at least having some views on it. We, of course, are following what FCC has come out with. We still feel that are several challenges with L-band. As -- first of all, it's not used. That frequency is not used anywhere in the world. That means that there are no equipment, no handsets and things like that, which you need an ecosystem. That's so important. But as with all frequencies and all the spectrum we're, of course, looking into it, and we have done it for several years. This is nothing new. I think that Ligado has been around for about 10 years. So it's nothing new.

So we are continuing -- our engineers are always looking into new development if something can happen. But so far, we have seen a little bit more headwind than anything else on that band.

**Operator**

The next question comes from Colby Synesael of Cowen.

**Colby Synesael** - *Cowen and Company, LLC, Research Division - MD & Senior Research Analyst*

Great. Two, if I may. First off, I was wondering if can you give us the number of customers that have stopped paying their bills, I guess, specifically their wireless bills as a result of COVID-19? And I assume that, that number was included in your disconnect. You'd mentioned, I think, 800,000 in response to Simon's question. Just trying to understand where that number comes into play.

And then secondly, as it relates to free cash flow and the dividend. I was wondering if you can just give us some framework in terms of how to think about the potential dividend payout expected in 2020?

**Hans Vestberg** - *Verizon Communications Inc. - Chairman & CEO*

You can start if you unmute.

**Matt Ellis** - *Verizon Communications Inc. - EVP & CFO*

Sorry about that. Thanks, Colby. So the number of customers who are referred to in the prior question was the number of customers who have told us their ability to pay their bills has been impacted by COVID. That's not to say they've been disconnected. They haven't been disconnected. Just like every other customer that doesn't pay completely on time that we work with them. And the vast majority of those, we end up getting them back on a payment schedule, and they continue their relationship with us. So we haven't -- and even those who have -- prevailed themselves of that doesn't necessarily mean that they have completely stopped paying. They are just indicating to us that they've seen an impact.

But when you look at the total impact we've seen, when I compare it to some of the numbers reported by -- whether it be on the mortgage side or the auto loan side, we're seeing a better overall performance in terms of the customer payment profile than what we've seen. And that's consistent with what we saw in the financial crisis in 2008 as well. I mean we have a very important product for our customers, and they value it. They value the connection they get from the best network, and we see those show up in the payment.

So Hans, I think you wanted to make some comments around the second question on free cash flow?



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**Hans Vestberg** - Verizon Communications Inc. - Chairman & CEO

Yes. First of all, I think we talked about where we stand on the balance sheet and the great work the team has done with the balance sheet, not only the last couple of years, but also in the first quarter. And we feel that we're in a very good position with our balance sheet, and that can be seen, that we both increased our CapEx this quarter as well as made the acquisition of BlueJeans. We have our capital allocation priorities, very clear for us: Number one is the business. Number two is the shareholders. Three is the debt reduction and number four is the buyback. And we feel that we're in a really good situation to continue to put our Board in the right position to serve our shareholders with dividend. But as we said on the Investor Day, when it comes to buybacks, that's probably unlikely happening this year given the situation. But all other priorities, we are definitely in a very good position to serve at this moment.

**Operator**

The next question comes from Michael Rollins of Citigroup.

**Michael Rollins** - Citigroup Inc, Research Division - MD & U.S. Telecoms Analyst

Just a couple of follow-ups. First, you gave a lot of detail on the potential impacts on revenue. I was curious if you could provide some additional details to quantify or help to approximate the variability of wireless expenses to the variability of gross adds or overall device sales?

And then secondly, does the temporary use of other license holder's spectrum increase Verizon's interest to rent or lease spectrum on a commercial basis in the future?

**Matt Ellis** - Verizon Communications Inc. - EVP & CFO

Thanks, Mike. So I'll answer the first question on the variability of expenses. So obviously, as we have lower volumes, you see lower handset costs and that obviously flows through immediately. But a lot of the other expenses, as you think about it in the immediate term, don't necessarily move. Even promo costs, for example, as we've talked about before, we now, under 606, amortize a lot of the promo expense over the expected life. So you see that come across over 2.5 years typically versus an immediate cost. So if we get a reduction, that benefit of lower promo expenses also gets amortized over that time period in the income statement. So you're going to see that flow through there.

Other areas where you see an impact from volumes, where we have lower volumes, especially in store, we see lower accessory sales, and those typically have a good margin on. We -- and so there are impacts there as well from seeing lower sales, not just in terms of lower expenses, but there is an impact on the revenue line that can come with that.

So net-net, you do see a reduction in cost with lower volumes, but there's some other things that go in the other direction and some of the benefits in expense are going to get realized over time rather than immediately in there. So hopefully, that helps you think around how that shows up in the income statement.

Hans, I'll let you add -- follow up on the question on the spectrum that we took advantage of.

**Hans Vestberg** - Verizon Communications Inc. - Chairman & CEO

Yes. First of all, we want to thank the FCC for so rapidly come out and lending out spectrum to all the players in the market because nobody knew how the usage will be on the network. As you can see, when we exclude the temporary spectrum that we lent from FCC, we have the same headroom, and the network has performed very well. On top of that, we are, of course, adding capacity right now and also put in the DSS, the dynamic spectrum sharing, which I can report that the tests are going very well. We're on plan for putting that opportunity in the hands of Tami and Ronan to decide when they want to turn on nationwide. So I think we have a very good spectrum strategy and with the spectrum we have, and we're very happy with it, and we're going to continue with that. So I think that's where we are right now.



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#### Operator

Your last question comes from Jennifer Fritzsche of Wells Fargo.

**Jennifer Fritzsche** - *Wells Fargo Securities, LLC, Research Division - MD & Senior Analyst*

Hans, I just wanted to follow-up on your DSS comments. So if I go back to my notes from mid-February following the Analyst Day, it seemed like you were very firm in saying DSS by year-end -- 5G by year-end with DSS. Is there any change to that?

And then just on the infrastructure behind it, you also talked about -- or Kyle talked about 5x the amount of small cells for 5G this year. Has any of the shifts, given the changes in social patterns, shifted back the macro there?

**Hans Vestberg** - *Verizon Communications Inc. - Chairman & CEO*

Thank you, Jennifer. First of all, we feel good about the dynamic spectrum sharing. It's -- we are continue to do the test and deploying equipment and the hardware in the field that is needed for doing that. I'm certain that Kyle and his team will put it in the hands of Ronan and Tami and decide when they turn it on in the second half. That's where we are today. So we're not have any supply issues to doing that or supply chain issues.

The same go for the 5x more -- 5G ready base station this year. We continue to just accelerate. And Kyle actually said publicly that we were ahead of the plan when we ended March. I can say today, we're still on plan on that 5x. We have no supply chain issues. We have, of course, complications with some municipalities, but our team is all around that and working with municipalities, finding new way, digital approval, things that we never thought were -- digital permitting processes, et cetera, which we never thought were possible.

So all in all, we are not giving up on those targets. And so far, it looks really good. And that's how a company should execute in times like this, managing the crisis, seeing that it will be a new -- and rethink how the new normal will look like. And that's what my team is doing every day right now, and we are very focused on doing that. And the good thing is that we feel good about our strategy where it stands.

**Brady Connor** - *Verizon Communications Inc. - SVP of IR*

And thanks, Hans and team. And everybody, make sure you stay safe and be well. And with that, we'll conclude the call.

#### Operator

Ladies and gentlemen, this does conclude the conference call for today. Thank you for your participation and for using Verizon Conference Services. You may now disconnect.

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